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TO: COUNCILMEMBERS

FROM: Irvin Corley, Jr., Fiscal Analyst ICJ.
Anne Marie Langan, Deputy Fiscal Analyst AML

DATE: January 30, 2006

RE: The Amended Neighborhood Enterprise Zone (NEZ) Act and its Ramifications to the City and Homeowners in Neighborhoods not in the Proposed NEZs

Statement

The Administration has not yet presented the City Council with a clear case as to how reducing property tax rates in certain neighborhoods will create growth in population or monetary value for the city.

Potential Fiscal Impact per the Amended NEZ Act

Using base information received from the Administration this past summer; we have generated data and charted how this proposal will reduce the amount of property tax the city collects by $365 million in the next 17 years. This analysis assumes the accuracy of the newspaper report that the administration's plan is to include 47 neighborhoods over a 3 three-year period. While the administration was helpful with providing the initial data on this proposal, the Assessor's Office staff has not yet commented on our analysis.

Replacing $365 million, an average of $22 million each year, would require residents to generate an additional $880 million in income each year in order to provide income tax revenue to supplant the lost property tax. If the responsibility was on the entire city population it would average out to $1,000 more in income per citizen. If it was simply applied to the 38,305 homeowners who have and are estimated to purchase homes in the proposed NEZs, it would be $23,000 more in income per household.

Proposed New NEZ Neighborhood Areas

The Assessor's Office staff provided a list of 25 neighborhoods originally but has not provided information on the remaining 22 areas. The list of 25 proposed in the summer were Arden Park, Aviation, Bagley, Berry Subdivision, Boston-Edison, East English Village, Golf Club, Golf Club Addition, Grandmont 1, Grandmont 2, Green Acres 1, Green Acres 2, Indian Village, LaSalle Garden, Livernois, Longfellow, Oakman East, Oakman West, Outer Drive, Palmer Woods, Rosedale 1, Rosedale 2, Russell Woods, Sherwood Forest, Virginia Park.

Analysis

On every house sold in an NEZ the city will lose 50% of the operating tax dollars that normally would have been collected. The homeowner will see a reduction in the overall millage rate of 22%. There is no housing gain for the city, unlike the new construction NEZs. The new construction NEZs that exist have not resulted in a net population growth as the city continues to lose at the annual rate of 10,000 residents. (The argument could be made that the loss would have been even greater than the 10,000 if it were not for the existing new construction NEZs.)

Many articles and arguments about the frustrations of Proposal A reinforce the fact that a house assessment at sale can skyrocket, sometimes doubling, thereby doubling the amount of taxes that are collected on that particular house. The media then uses a real example of how the assessment "pop-up" value shocked the new homeowner who is not prepared for or anticipated the increase in taxes on the property.

The first problem in this assertion is that "all" of these assessment increases have generated a substantial growth in tax collections when in fact the city has averaged only a 3.8% annual increase in property valuations since Proposal A began in 1994. In fact, the Headlee Amendment which has affected so many other communities by making them roll back their operating millage because the dollars to be collected from taxes would exceed the prior year's collection by the legislated amount has never been a problem for the City of Detroit. The City of Detroit has only once had to roll back the operating millage and it was more of a mistake than a true Headlee rollback.

The second problem is that many new homeowners do not understand that since 1994 it doesn't matter what the current taxes on a house are. The taxes that the new homeowners will be paying will be based on the price they paid for the new home, and not the previous valuation. From that point on, the assessment will be increased by a rise in the Consumer Price Index not to exceed 5%. It appears that realtors and lenders may not be completely candid with home purchasers for fear of losing the sale. They seem to be willing to let the purchasers assume a lower than actual monthly cost based on the current taxes instead of factoring in the assessment "pop up" in order to fit the purchasers' budget, or the purchasers may not comprehend the explanation provided by the realtor or lenders.

The third problem is that no one has discussed how this will create a schism between existing neighborhoods and homeowners when one neighborhood is given the NEZ designation and the other isn't. False market conditions will be created distorting the values of houses that should be similarly priced.

"Old- home" NEZs will have a millage rate of 52 compared to 67. New-build NEZs have a millage rate of 16 compared to 67. Using the example of a recent $100,000 home sale, with a taxable value of $50,000, the tax on new construction will be $800 while the tax on the "old home" NEZ would be $2,600 compared with the tax in every other neighborhood at $3,350. So, instead of limiting the inequity that results from Proposal A, the inequity is expanded to a multi-tier situation, that no one will understand after an additional year or two.

Council should note that the City of Detroit portion of the levy is only 30.0201 mills or 44% of the total. The tax burden on Detroit residents compared to other cities results from the Board of Education, State School levy, Wayne County and others.

The tax rates break down as follows:

	Basic Tax	Percent of Total Levy	Old Neighborhood NEZ	New Construction NEZ
City Operating	19.9520	29.5%	9.9760	
Garbage Disposal	2.9928	4.4%	2.9928	
Debt Service	7.0753	10.5%	7.0753	
Library	4.6307	6.8%	4.6307	
Board of Ed	13.0000	19.2%	13.0000	
State School Tax	6.0000	8.9%	6.0000	
County	13.9861	20.7%	8.9621	
Total	**67.6369**	**100%**	**52.6369**	**16.0000**

While there is something inherently unfair about homeowners requesting the same services from the government and yet paying different rates for those services, a tiered system already exists in the city with new-construction NEZs, existing apartment buildings that are modified into condominiums, Renaissance Zones, Tax Increment Financing (TIF) Zones, Local Development Finance Authority (LDFA) and Act 198, 328 and 146 Tax Abatements for commercial businesses.

The old-home NEZ annual savings of $750 begins to create a new division and problem amongst homeowners in similarly aged, sized, styled and located neighborhoods.

If homeowners in one neighborhood are given a NEZ designation and tax break and an adjoining neighborhood with similarly styled/sized housing does not have the NEZ designation and tax break, an unfair market advantage is created for the homeowners in the NEZ for home sale purposes. First, they will have a better chance of selling and second; the homeowner may be able to sell at a higher price due to the value of the price break, as $750 over the 15-year NEZ period totals between $11,250 and $16,200 savings in taxes. This will of course dilute the benefit of the tax break to the buyer. The total amount of savings will depend on the increases in the taxable value over the 15 years and it cannot exceed 5% in any given year. It is also reasonable to suppose that houses in the non-NEZ neighborhoods will sell at a price lower than they would have prior to the NEZ to make up for the fact that the buyer will have to pay more in taxes than his neighbor across the street.

This condition will have a negative effect on assessments citywide which will offset any gains the city might have made with the sale price increases in these new NEZ neighborhoods.

The Far Eastside and Lower Eastside Neighborhoods' Proposal

Some of the far east and lower eastside neighborhoods that the Administration plans to include in the first round include East English Village, Indian Village and Berry Subdivision.

East English Village is a neighborhood group formerly known as DEAR, not a subdivision in the strict sense, formed in the 1970s along with a host of neighborhood groups around it (NEAR, ONE, AWARE, DARE). East English is sandwiched between ONE and Morningside (formerly NEAR) and bounded between I-94 and Mack Avenue. East English is a significantly smaller area because the groups were created at the time simply by using main or "busy" streets as boundaries. So Morningside goes all the way from Alter Road to East Outer Drive/Whittier; East English Village is from East Outer Drive/Whittier to Cadieux; ONE is from Cadieux to Moross. All three neighborhoods have similarly styled, sized and aged housing, mostly constructed between 1927 and 1950. Houses in all three areas are priced based on condition between $50,000 and $200,000.

So while all three neighborhood groups offer similarly sized, aged, styled housing, East English Village will get a boost that will make that housing stock more attractive to buyers who were considering the eastside in an established neighborhood in the first place.

Berry Subdivision and Indian Village have similarly styled, sized and aged housing that is unique to the eastside. Price wise, some of the condos along the river are similar and therefore those owners might be at a disadvantage when it comes to selling. However, condos and 3,500 sq. ft. historic homes are such different styles of living that the difference of 15 mills would not be as big of an issue.

Conclusion

Council needs to hear how the Administration hopes to make this tax break successful for the City of Detroit. Administrators from other cities have been interviewed and state that there is no way they can implement this tax break since costs for general city services are going up and this would give them less money to pay for these services. In most cities as it once was with Detroit, the main source of revenue for general operations is the property tax. Detroit only anticipates that 8% of the revenue will come from property tax.

Proposal A allowed long-time homeowners to stay in their homes and not be forced out due to unchecked growth in property values. Proposal A intended only to delay the increase in taxes until a future sale of the property, so as not to permanently reduce local governments revenue collections. The NEZ proposal for existing home sales will delay the collection revenue for another 17 years, revenues necessary to support city services. This is a loss the City of Detroit is not in a position to absorb. It also changed the taxing structure for schools that helped property values increase, because most of the cost of schools was shifted to sales tax. But it also created the "inequity" that neighbors in similar housing are paying very different-sized tax bills. The NEZ will create another tier of inequity that complicates the problem further. It also shifted an additional cost to families with school children since many activities that used to be covered through taxes paid by the entire community must now be born by the user due to Proposal A. So comparing tax rates by community becomes more difficult because you need to dig deeper and determine all user costs, if you want to compare the true cost of living.

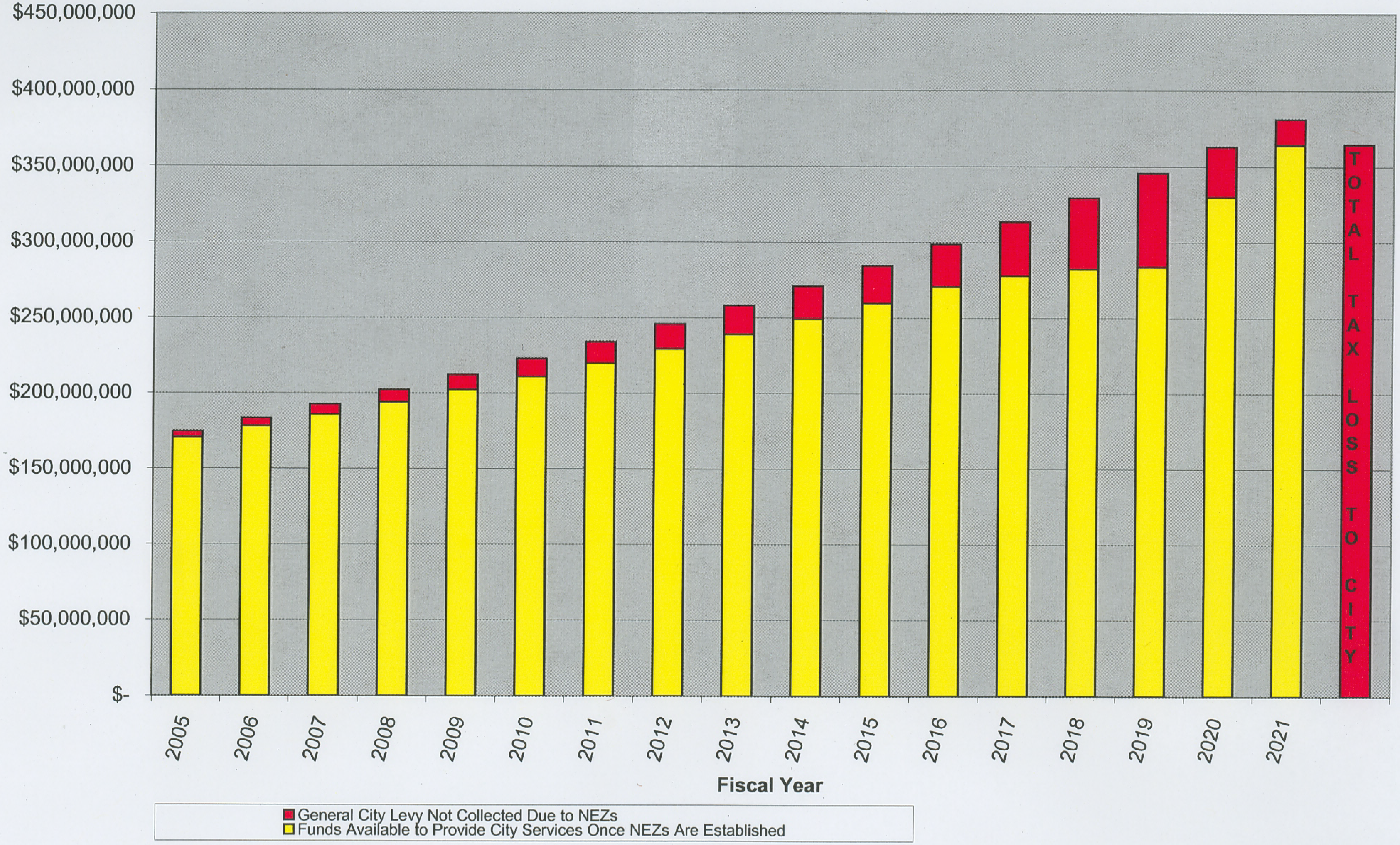
The inequity in property valuations created by Proposal A on home sales can be addressed by market conditions. The sale price of the home can be adjusted to reflect increased tax assessment. The expansion of the NEZ designation will only complicate the problem.

The administration has successfully argued the case to stop the state mandated rollback of the local income taxes due to the fiscal conditions of the city. The administration lobbied for and was successful in having the utility tax legislation changed to prevent a rollback in the utility users tax. Yet the administration pushed for the expansion of the NEZ designation from only new construction to existing home sales. Property tax is the least regressive of the three taxes. The administration's action on taxes appears to support regressive taxes over non-regressive taxes. Before Council follows the administration's lead, Council must decide if this is the best path for the future of the City. While there is no question that tax relief for the citizens is laudable, there is still a question if tax relief is currently possible, as revenues to fund basic city services are already insufficient.

Attachments
cc: Council Divisions
Auditor General
Ombudsperson
Matt Grady, Interim Finance Director
Roger Short, Budget Director
Julie Castone, Assessor
Anthony Adams, Deputy Mayor
Kandia Milton, Mayor's Office

Chart 1

Financial Analysis of Revised NEZ Act for Existing Neighborhoods



Analysis of Revised NEZ Act for Existing Neighborhoods

1.05

		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Total	Avg./year
PHASE I																				
Bldg. Tax Val.		$ 68,963	$ 72,411	$ 76,032	$ 79,833	$ 83,825	$ 88,016	$ 92,417	$ 97,038	$ 101,890	$ 106,984	$ 112,333	$ 117,950	$ 123,848	$ 130,040	$ 136,542			$ 1,488,122	
20 neighborhoods																				
97-04	5055	348,609,813	366,040,304	384,342,319	403,559,435	423,737,407	444,924,277	467,170,491	490,529,015	515,055,466	540,808,239	567,848,651	596,241,084	626,053,138	657,355,795	690,223,585			7,522,499,017	
1	700	48,274,100	50,687,805	53,222,195	55,883,305	58,677,470	61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			1,041,685,737	
2	700		50,687,805	53,222,195	55,883,305	58,677,470	61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			993,411,637	
3	700			53,222,195	55,883,305	58,677,470	61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			942,723,832	
4	700				55,883,305	58,677,470	61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			889,501,636	
5	700					58,677,470	61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			833,618,331	
6	700						61,611,344	64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			774,940,861	
7	700							64,691,911	67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			713,329,517	
8	700								67,926,507	71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			648,637,606	
9	700									71,322,832	74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			580,711,100	
10	700										74,888,973	78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			509,388,268	
11	700											78,633,422	82,565,093	86,693,348	91,028,015	95,579,416			434,499,294	
12	700												82,565,093	86,693,348	91,028,015	95,579,416			355,865,872	
13	700													86,693,348	91,028,015	95,579,416			273,300,779	
14	700														91,028,015	95,579,416			186,607,431	
15	700															95,579,416			95,579,416	
Taxable Val.		396,883,913	467,415,914	544,008,905	627,092,655	717,124,758	814,592,339	920,013,867	1,033,941,067	1,156,960,953	1,289,697,974	1,432,816,294	1,587,022,202	1,753,066,660	1,931,748,009	2,123,914,825			16,796,300,335	
Mill reduction		0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0124700	0.0149640	0.0174580				
Tax loss to City		$ 3,959,314	$ 4,662,941	$ 5,427,033	$ 6,255,876	$ 7,154,037	$ 8,126,373	$ 9,178,058	$ 10,314,596	$ 11,541,842	$ 12,866,027	$ 14,293,775	$ 15,832,133	$ 21,860,741	$ 28,906,677	$ 37,079,305			$ 197,458,730	$ 13,163,915
Op. mill reduction		0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.625	0.75	0.875				
Current Op. mill		0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952				
PHASE II		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020		total	
			$ 72,411	$ 76,032	$ 79,833	$ 83,825	$ 88,016	$ 92,417	$ 97,038	$ 101,890	$ 106,984	$ 112,333	$ 117,950	$ 123,848	$ 130,040	$ 136,542	$ 143,369			
15 neighborhoods																				
97-05	4300		$ 311,367,945	326,936,342	343,283,159	360,447,317	378,469,683	397,393,167	417,262,826	438,125,967	460,032,265	483,033,879	507,185,573	532,544,851	559,172,094	587,130,698	616,487,233			
1	540		39,102,021	41,057,122	43,109,978	45,265,477	47,528,751	49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		843,765,447	
2	540			41,057,122	43,109,978	45,265,477	47,528,751	49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		804,663,426	
3	540				43,109,978	45,265,477	47,528,751	49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		763,606,304	
4	540					45,265,477	47,528,751	49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		720,496,325	
5	540						47,528,751	49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		675,230,848	
6	540							49,905,188	52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		627,702,097	
7	540								52,400,448	55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		577,796,909	
8	540									55,020,470	57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		525,396,461	
9	540										57,771,494	60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		470,375,991	
10	540											60,660,068	63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		412,604,497	
11	540												63,693,072	66,877,725	70,221,612	73,732,692	77,419,327		351,944,429	
12	540													66,877,725	70,221,612	73,732,692	77,419,327		288,251,357	
13	540														70,221,612	73,732,692	77,419,327		221,373,631	
14	540															73,732,692	77,419,327		151,152,019	
15	540																77,419,327		77,419,327	
Taxable Val.			39,102,021	82,114,244	129,329,934	181,061,908	237,643,755	299,431,131	366,803,135	440,163,762	519,943,444	606,600,685	700,623,791	802,532,706	912,880,953	1,032,257,693	1,161,289,905		7,511,779,067	
Mill reduction			0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0124700	0.0149640	0.0174580			
Tax loss to City			$ 390,082	$ 819,172	$ 1,290,195	$ 1,806,274	$ 2,370,734	$ 2,987,125	$ 3,659,228	$ 4,391,074	$ 5,186,956	$ 6,051,448	$ 6,989,423	$ 8,006,066	$ 11,383,625	$ 15,446,704	$ 20,273,799		$ 91,051,906	$ 6,070,127
Op. mill reduction			0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.625	0.75	0.875			
Current Op. mill			0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952			
PHASE III		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	TOTAL	Avg./year
			$ 72,411	$ 76,032	$ 79,833	$ 83,825	$ 88,016	$ 92,417	$ 97,038	$ 101,890	$ 106,984	$ 112,333	$ 117,950	$ 123,848	$ 130,040	$ 136,542	$ 143,369	$ 150,538		
12 neighborhoods																				
97-06	3900			296,523,659	311,349,842	326,917,334	343,263,201	360,426,361	378,447,679	397,370,063	417,238,566	438,100,495	460,005,519	483,005,795	507,156,085	532,513,889	559,139,584	587,096,563	6,398,554,637	
1	430			32,693,634	34,328,316	36,044,732	37,846,968	39,739,317	41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	705,481,665	
2	430				34,328,316	36,044,732	37,846,968	39,739,317	41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	672,788,031	
3	430					36,044,732	37,846,968	39,739,317	41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	638,459,715	
4	430						37,846,968	39,739,317	41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	602,414,983	
5	430							39,739,317	41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	564,568,015	
6	430								41,726,283	43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	524,828,698	
7	430									43,812,597	46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	483,102,416	
8	430										46,003,227	48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	439,289,819	
9	430											48,303,388	50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	393,286,592	
10	430												50,718,557	53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	344,983,204	
11	430													53,254,485	55,917,209	58,713,070	61,648,723	64,731,160	294,264,647	
12	430														55,917,209	58,713,070	61,648,723	64,731,160	241,010,162	
13	430															58,713,070	61,648,723	64,731,160	185,092,953	
14	430																61,648,723	64,731,160	126,379,883	
15	430																	64,731,160	64,731,160	
Taxable Val.				32,693,634	68,656,632	108,134,195	151,387,873	198,696,584	250,357,695	306,688,177	368,025,812	434,730,491	507,185,573	585,799,336	671,006,512	763,269,908	863,082,127	970,967,393	6,280,681,942	
Mill reduction				0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0099760	0.0124700	0.0149640	0.0174580		
Tax loss to City				326,152	684,919	1,078,747	1,510,245	1,982,197	2,497,568	3,059,521	3,671,426	4,336,871	5,059,683	5,843,934	6,693,961	9,517,976	12,915,161	16,951,149	76,129,510	5,075,301
Op. mill reduction				0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.625	0.75	0.875		
Current Op. mill				0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952	0.019952		
Tax Loss due to 47 Neighborhoods NEZs		3,959,314	5,053,023	6,572,356	8,230,990	10,039,057	12,007,353	14,147,380	16,471,393	18,992,437	21,724,408	24,682,095	27,881,240	35,710,742	46,984,264	62,043,985	33,188,960	16,951,149	364,640,146	
General City Levy		$174,576,611	$ 183,305,442	$ 192,470,714	$ 202,094,249	$ 212,198,962	$ 222,808,910	$ 233,949,355	$ 245,646,823	$ 257,929,164	$ 270,825,622	$ 284,366,904	$ 298,585,249	$ 313,514,511	$ 329,190,237	$ 345,649,749	$ 362,932,236	$ 381,078,848	$ 4,511,123,585	
Funds Available for City Services once NEZs are Established		$170,617,297	$ 178,252,419	$ 185,898,357	$ 193,863,259	$ 202,159,905	$ 210,801,557	$ 219,801,975	$ 229,175,431	$ 238,936,727	$ 249,101,214	$ 259,684,808	$ 270,704,009	$ 277,803,770	$ 282,205,973	$ 283,605,764	$ 329,743,276	$ 364,127,699	$ 4,146,483,440	
		2.268%	2.757%	3.415%	4.073%	4.731%	5.389%	6.047%	6.705%	7.363%	8.022%	8.680%	9.338%	11.390%	14.273%	17.950%	9.145%	4.448%	8.083%	

Chart 2

City's Real Property Valuation and the Percentage Change of Valuation